Supreme Court, U.S.
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NO. 04-252

IN THE

Supreme Court of the United States

MACY'S EAST, INC.,
Petitioner,

v.

COMMISSIONER OF REVENUE,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME JUDICIAL COURT OF THE COMMONWEALTH OF MASSACHUSETTS

BRIEF IN OPPOSITION OF MASSACHUSETTS COMMISSIONER OF REVENUE

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1. Whether the Respondent Massachusetts Commissioner of Revenue, by determining as a matter of Massachusetts tax law that Petitioner Macy's East, Inc. was not entitled to carry forward and deduct certain net operating losses, violated the supremacy clause "by depriving Macy's East of valuable property rights of its estate in bankruptcy," notwithstanding the well-settled rule that a debtor's property rights in bankruptcy proceedings are determined by applicable non-bankruptcy law, *see Butner v. United States*, 440 U.S. 48 (1979).

2. Whether the mere fact that Massachusetts tax law differs from federal tax law in the treatment of certain net operating losses creates a federal question reviewable by the Court.

3. Whether Macy's East, which operated eleven retail stores in Massachusetts during the tax year at issue, was subjected to an extraterritorial tax in violation of the due process and commerce clauses when the Massachusetts Commissioner of Revenue applied the state statutory formula to determine that some of Macy's East's corporate income was reasonably related to activities conducted within Massachusetts.

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Jurisdiction

Jurisdiction to review the first and third questions presented rests upon 28 U.S.C. § 1257(a). However, contrary to Petitioner's contention, the Court does not have jurisdiction over the second question presented because the mere fact that Massachusetts tax law differs from federal tax law in the treatment of certain net operating losses does not create a federal claim.

Facts

For purposes of this Brief in Opposition to the Petition for a Writ of Certiorari, the Respondent Massachusetts Commissioner of Revenue accepts and incorporates by reference the facts set forth in the decision of the Massachusetts Supreme Judicial Court, *Macy's East, Inc. v. Commissioner of Revenue*, 441 Mass. 797, 808 N.E.2d 1244 (2004) (reproduced in the Appendix to the Petition for a Writ of Certiorari ("Pet. App.") at 1a-18a), and the decision of the Massachusetts Appellate Tax Board (reproduced in Pet. App. at 20a-46a).

Reasons for Denying the Writ

The Petition should be denied. The first and third claims present no issues meriting the Court's attention and are, in any event, meritless. *See* Supreme Court Rule 10 ("[r]eview on a writ of certiorari is not a matter of right, but of judicial discretion" and a petition "will be granted only for compelling reasons"); *In Re Woods*, 143 U.S. 202, 206 (1892) (purpose of certiorari jurisdiction is to permit the Court to select cases of "gravity and general importance"). The second claim presents no constitutional question

and thus is not reviewable by the Court. *See* 28 U.S.C. § 1257(a).

Petitioner Macy's East, Inc. ("Macy's East") asks the Court to review three questions relating to the Respondent Massachusetts Commissioner of Revenue's ("Massachusetts Commissioner") treatment of premerger net operating losses ("NOLs") generated by four entities Macy's East absorbed in various mergers. *See* Pet. at i, 2-29; Pet. App. at 2a. For federal tax purposes, the relevant and then-applicable provisions of the Internal Revenue Code allowed Macy's East to carry forward and deduct the NOLs at issue. Pet. App. at 8a. However, the Massachusetts Commissioner determined that, for state corporate excise tax purposes, Massachusetts law did not allow Macy's East to carry forward and deduct the NOLs. Pet. App. at 2a-3a; *see* Mass. Gen. Laws ch. 63, § 30(5)(a), as appearing in St. 1992, c. 133, § 403; 830 Code Mass. Regs. § 63.30.2(11), adopted on January 1, 1993. The primary issue raised and decided below was whether the Commissioner's position was correct as a matter of state law. *See* Pet. App. at 1a-46a. Both the Massachusetts Appellate Tax Board and the Supreme Judicial Court concluded that it was. *See id.*

In its Petition, Macy's East attempts to transform its displeasure with Massachusetts tax law into wrongs of constitutional dimension. One result of this exercise is a Petition that ignores the fundamental difference between state and federal law, even to the point of asking the Court to review the question whether Massachusetts has misinterpreted its own tax statute. *See* Pet. at 18-25. Another result is a Petition that is long on tax and bankruptcy policy arguments and short on any of the accepted justifications for plenary review. *See* Supreme Court Rule 10. Moreover, the claims are without merit. As stated more fully below, the Petition should be denied.

I. THE PETITION'S BANKRUPTCY LAW CLAIM DOES NOT MERIT PLENARY REVIEW.

Macy's East first alleges that, because the NOLs at issue were "assets" of the bankruptcy estates of the debtor corporations, Massachusetts tax law violates the supremacy clause "by depriving Macy's East of valuable property rights of its estate in bankruptcy." Pet. at i and 15-18. This claim does not merit plenary review. The Massachusetts Supreme Judicial Court correctly recognized that the claim failed in the face of the well-settled principle of bankruptcy law that "[t]he nature and extent of the debtor's interest in property is determined by applicable non-bankruptcy law, or State law." Pet. App. at 16a (internal citation and quotation marks omitted) (citing *Butner v. United States*, 440 U.S. 48, 54 (1979)). Because Macy's East could not, under state law, carry forward and deduct the NOLs, the NOLs were never part of the Macy's East bankruptcy estate, and there was, accordingly, no deprivation of any property interest. Pet. App. at 16a-17a.

The Petition's only response to *Butner* is to insist that the instant case is different because "there is no state law that would deprive Macy's East of its property right in its NOLs." Pet. at 4 n.1. In fact, Massachusetts law regarding premerger NOLs has been articulated by all three branches of state government: the Legislature, which enacted Mass. Gen. Laws ch. 63, § 30(5)(a); the Executive, whose appointee the Commissioner of Revenue promulgated 830 Code Mass. Regs. § 63.30.2(11); [1] and the Supreme Judicial Court, which

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[1] In Massachusetts, administrative regulations have the full force of law. *See Haverty v. Commissioner of Correction*, 437 Mass. 737, 758, 776 N.E.2d 973, 987 (2002).

endorsed the Commissioner's position, *see* Pet. App. at 1a-8a. The rule of *Butner* thus reduces the bankruptcy-law claim to a complaint about how Massachusetts interprets its own law. Such a claim is reviewable by this Court only in "extreme circumstances." *See Mullaney v. Wilbur*, 421 U.S. 684, 691 (1975). As *Butner* itself teaches, the "the happenstance of bankruptcy" does not constitute such an extreme circumstance. *See Butner*, 440 U.S. at 55 (internal quotation marks omitted);[2] *contrast Lucas v. South Carolina Coastal Council*, 505 U.S. 1003 (1992); *Fairfax's Devisee v. Hunter's Lessee*, 11 U.S. (7 Cranch) 603 (1813).

Apart from the merits, the Petition fails to present a compelling case for plenary review. Macy's East does not claim that the Massachusetts Supreme Judicial Court applied the *Butner* principle "in a way that conflicts with the decision of another state court of last resort or of a United States court of appeals." *See* Supreme Court Rule 10(b). Furthermore, the Petition's parade of horribles -- for example, that disallowing NOLs conflicts with the spirit of the bankruptcy law[3] and that differing state laws regarding NOLs will

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[2] Indeed, the *Butner* Court noted that to treat property interests differently based on federal bankruptcy status could encourage forum shopping and create a "windfall" for debtors. *Butner*, 440 U.S. at 55.

[3] While federal bankruptcy law may readily prevail over state bankruptcy law, *see International Shoe Co. v. Pinkus*, 278 U.S. 261, 268 (1929), non-bankruptcy state law is suspended "only to the extent of actual conflict with the system provided by the Bankruptcy Act of Congress." *Butner*, 440 U.S. at 54 n.9. Furthermore, a "presumption against preemption" applies in the circumstances of this case, in which the historic police power of the Commonwealth of Massachusetts to maintain its own system of taxation is alleged to

confuse bankruptcy participants and hinder reorganization -- are arguments that the Court has already rejected, in *Butner*. *See Butner*, 440 U.S. at 54-58. In sum, the Petition's bankruptcy-law claim does not merit plenary review.

II. THE COURT LACKS JURISDICTION OVER THE PETITION'S *LIBSON SHOPS* CLAIM BECAUSE THERE IS NO CONSTITUTIONAL REQUIREMENT THAT STATE TAX LAW CONFORM TO FEDERAL TAX LAW.

Macy's East next asks the Court to review whether the decision below "violates the principle set out by this Court in *Libson Shops, Inc. v. Koehler*, 353 U.S. 382 (1957)." Pet. at i and 18-25. Macy's East forgets that the Court's authority under 28 U.S.C. § 1257(a) "is limited to enforcing the commands of the United States Constitution." *MuMin v. Virginia*, 500 U.S. 415, 422 (1991); *see also Dickerson v. United States*, 530 U.S. 428, 438 (2000) ("It is beyond dispute that we do not hold a supervisory power over the courts of the several States."). In *Libson Shops*, the Court addressed the treatment of premerger NOLs under the Internal Revenue Code; the Court did not address any constitutional issues. *See Libson Shops*, 530 U.S. at 382. As the Constitution does not require that state tax law conform to federal tax law, the mere fact that Massachusetts and other States have declined to follow *Libson Shops* or the Internal Revenue Code does not create a federal claim reviewable by the Court. Accordingly, the Court lacks jurisdiction

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be in conflict with federal law. *See New York v. Federal Energy Regulatory Comm'n*, 535 U.S. 1, 17-18 (2002).

over the Petition's *Libson Shops* claim under 28 U.S.C. § 1257(a).[4]

The Petition's attempts to federalize this claim fall flat. The Petition acknowledges, as it must, that "states are free to enact tax laws that explicitly limit NOLs availability." Pet. at 25. Nonetheless, the Petition alleges that "where there is no explicit [state] statutory provision and the states' tax laws conform to federal tax law,[5] the *Libson Shops* doctrine and IRC section 381 should apply." Pet. at 25. While the Petition does not expressly invoke the Constitution, suffice it to say that this case does not come close to being one of those rare instances where the Court should inquire whether a State's interpretation of its own law is so far beyond what a fair reading of the state law would permit as to constitute a denial of due process. *See, e.g., Bouie v. City of Columbia*, 378 U.S. 347 (1964) (reversing criminal trespass convictions of African-American "sit-in" demonstrators because the South Carolina supreme court's construction of state trespass law was so unexpected and indefensible

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[4] Furthermore, the Petition misunderstands the import of *Libson Shops* as a matter of federal law. The case established a "continuity of business enterprise" limitation on the use of federal NOL carry-overs, not an affirmative grant of authority for their use by a merger successor. *See Libson Shops*, 353 U.S. at 385-86 (finding it "unnecessary to discuss" whether the Internal Revenue Code as it then existed allowed such carry-overs because in any event the required continuity of business enterprise was lacking). Authority to carry forward certain NOLs for federal tax purposes was explicitly established by 1954 amendments to the Internal Revenue Code that added sections 381 and 382. *See* Pet. at 21.

[5] While state law may incorporate by reference federal statutes or common-law principles, clearly a State does not actually apply federal law to determine whether a state tax is due.

as to deny the demonstrators their constitutional due process right to sufficient notice that their conduct was criminal).

In any event, the decision below, in addition to being presumptively correct, *see Bush v. Gore*, 531 U.S. 98, 112 (2000) (Rehnquist, C.J., concurring), was manifestly correct as a matter of state law. As the Massachusetts Supreme Judicial Court found, the Commissioner's position was supported by statute and regulation and was consistent with the case law recognizing that "Massachusetts tax law can and does depart from Federal tax law, particularly in matters authorizing deductions for prior year's losses." Pet. App. at 9a (citing, e.g., *Bill DeLuca Enters., Inc. v. Commissioner of Revenue*, 431 Mass. 314, 325, 727 N.E.2d 508, 516 (2000)).

Furthermore, it is unsurprising that the States have expressed varying views on the tax treatment of premerger NOLs, given that each State applies its own tax law to the issue. *See* Pet. at 23-25, and cases cited therein. The cited cases provide no justification for plenary review because they do not evidence a conflict over an important federal question, as required by Supreme Court Rule 10(b).[6] In sum, the Court should not consider the Petition's *Libson Shops* claim.

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[6] Moreover, none of the cited cases addressing premerger NOLs makes reference to any bankruptcy proceedings. *See* Pet. at 15-18 (bankruptcy-law claim).

III. THE PETITION'S EXTRATERRITORIAL TAXATION CLAIM DOES NOT MERIT PLENARY REVIEW.

Lastly, Macy's East alleges that the decision below subjected it to extraterritorial taxation in violation of the due process and commerce clauses of the United States Constitution. Pet. at i and 26-29. During the tax year at issue, Macy's East operated eleven retail stores in Massachusetts. Pet. App. at 3a, 22a. Macy's East's Massachusetts component of its excise tax return reported $201 million of income attributable to Massachusetts for that tax year as calculated according to the Massachusetts statutory apportionment formula, which considers in-state sales, property, and payroll. Pet. App. at 43a-44a; *see* Mass. Gen. Laws ch. 63, § 38. Macy's East then sought an abatement, claiming that, based on its separate accounting analysis, the denial of net operating loss deductions resulted in unconstitutional extraterritorial taxation because all but one of the Macy's East Massachusetts stores had generated losses during the year at issue. Pet. App. at 17a, 42a-43a.

This claim does not merit plenary review. Contrary to the Petition's allegation, the Massachusetts Supreme Judicial Court did not "ignore" relevant Supreme Court precedent. *See* Pet. at 29. The court below simply agreed with the Massachusetts Commissioner and the Appellate Tax Board that, under the circumstances of this case, Macy's East's accounting theories failed to show that the Massachusetts apportionment formula resulted in unconstitutional taxation. Pet. App. at 17a, 42a-44a (citing *Gillette Co. v. Commissioner of Revenue*, 425 Mass. 670, 679-81, 683 N.E.2d 270, 277-78 (1997), in turn citing *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159 (1983)). Thus, any decision by this Court in Macy's East's favor would amount to little more than the correction

of erroneous factual findings or the misapplication of a properly stated rule of law. *See* Supreme Court Rule 10 (plenary review "rarely granted" to correct such errors).

Furthermore, the claim is without merit. The Massachusetts apportionment formula need only produce "a 'rough approximation' of the corporate income that is 'reasonably related to the activities conducted within the taxing state.'" *See Exxon Corp. v. Wisconsin Dep't of Revenue*, 447 U.S. 207, 223 (1980) (quoting *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 273 (1978)). The Massachusetts Supreme Judicial Court correctly determined that Macy's East, through its separate accounting analysis, failed to meet its "distinct burden of showing by 'clear and cogent evidence' that [the state tax] results in extraterritorial values being taxed." *See Container Corp.*, 463 U.S. at 164 (quoting *Exxon*, 447 U.S. at 221); Pet. App. at 17a, 42a-44a. Indeed, this Court has itself expressed reservations about the use of separate accounting for purposes of state taxation. *See Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 438 (1980) (noting that separate accounting is "not constitutionally required," in part because it is often "misleading to characterize the income of the business as having a single identifiable 'source'"). In sum, the Petition's extraterritorial taxation claim does not merit plenary review.

Conclusion

For all of the reasons stated above, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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